

STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

ILLINOIS INDEPENDENT TELEPHONE)	
ASSOCIATION)	
)	00-0233
Petition for initiation of an investigation)	
of the necessity of and the establishment)	
of a Universal Service Support Fund)	
in accordance with Section 13-301(d))	
of the Public Utilities Act)	
)	
ILLINOIS COMMERCE COMMISSION)	
ON ITS OWN MOTION)	
)	00-0335
Investigation into the necessity of and,)	
if appropriate, the establishment of a)	
universal support fund pursuant to)	
Section 13-301(d) of the Public Utilities Act.)	

REBUTTAL TESTIMONY OF
CATE HEGSTROM
ON BEHALF OF
AT&T COMMUNICATIONS OF ILLINOIS, INC.

AT&T Exhibit 5.0

May 31, 2001

OFFICIAL FILE

ILL. C. C. DOCKET NO. 00-0233/0335

AT&T Date Filed 7-20-01 Exhibit No. 5.0

Witness _____

Date 7-20-01 Report: CB

1 **Q. Please state your name and business address.**

2 A. My name is Cate Hegstrom. My business address is 222 West Adams St., Suite
3 1500, Chicago, IL 60606.

4
5 **Q. Are you the same Cate Hegstrom that prefled direct testimony on May 11,**
6 **2001 in these proceedings?**

7
8 A. Yes, I am.

9
10 **Q. What is the purpose of your rebuttal testimony?**

11 A. The purpose of my testimony is to respond to the direct testimony of Staff
12 regarding its proposed methodology for calculating the potential size of a state
13 high cost fund pursuant to Section 13-301(d) of the Illinois PUA. In doing so, I
14 will also respond to the supplemental direct testimony of Mr. Schoonmaker,
15 specifically regarding the appropriate size of an initial Illinois state high cost
16 fund. To the extent that the revised methodology I propose herein results in a
17 specific LEC being ineligible for fund support, my testimony can be considered a
18 rebuttal to that company's request for fund support. Additionally, I respond to the
19 testimony of Ameritech Illinois and Verizon regarding the issue of the true-up to
20 the DEM Weighting Funds in effect from 1998 through the present, which the
21 Commission specifically requested be addressed in this phase of these
22 consolidated dockets.

23

1 Dr. Clarke is also providing rebuttal testimony, responding specifically to Staff
2 witness Mr. Robert Koch concerning modifications to HAI Model 5.0a input
3 values.

4
5 **Q. Please summarize the results of your analyses as to the potential size of an**
6 **initial state high cost fund pursuant to Section 13-301(d).**

7
8 **A.** The Commission has numerous proposals to consider in establishing an
9 appropriate methodology by which a Section 13-301(d) fund might be sized. At
10 the one extreme, Mr. Schoonmaker has proposed an initial fund the size of
11 \$14,567,114. However, as I discuss below, the calculations Mr. Schoonmaker
12 employs are not compliant with the requirements of Section 13-301(d). Using
13 compliant assumptions and methodologies, use of Mr. Schoonmaker's calculated
14 HAI 5.0a economic costs could support a fund sized between \$10,964,234 and
15 \$11,959,239.

16
17 If the Commission disallows the modifications to the HAI 5.0a input values Mr.
18 Schoonmaker implemented, and instead relies on the default values of the model,
19 an initial fund sized at approximately \$9,327,145 could result.

20
21 My final analyses, based on the Commission adoption of Dr. Clark's
22 recommended modifications to the HAI 5.0a input values, would result in an
23 initial fund sized between \$7,087,590 and \$6,299,613.

1 Due to the complexity of issues and calculations, including the issue of an
2 affordable rate, all of these fund sizes may be modified and/or reduced. Once the
3 Commission adopts a methodology, certain factors would need to be updated, as
4 required by Section 13-301(d).

5
6 **Q. Ms. Hegstrom, after reviewing the direct testimony filed by other parties in**
7 **these proceedings, are there any issues on which the parties are in**
8 **agreement?**

9
10 **A.** Yes. There are two specific issues on which the parties agree. The first issue
11 concerns the basis for assessing the funding carriers' fund obligations. All parties
12 have supported the use of intrastate retail revenues. The second issue concerns
13 the method of recovery of fund obligations. All parties support the use of an end
14 user surcharge, assessed as a separate line item on the end users' bills.
15 Additionally, although I did not address it in my direct testimony, I concur in the
16 recommendations that ISCECA be appointed the administrator of any fund
17 initially established pursuant to Section 13-301(d) as a result of these proceedings.
18 Because there is no disagreement on these issues, I would recommend issues
19 related to the potential implementation be discussed in a Staff-chaired meeting
20 within the next month, as discussed in the Comments filed March 14, 2001 by
21 Staff. The list of issues would also include those mentioned by some parties,
22 including the limits for costs of administering the fund, the frequency of
23 surcharge updates, frequency of fund remittances and distributions, and processes
24 to deal with fund shortfalls and excesses.

1 **Q. Are there other issues of agreement among the parties?**

2
3 A. No. Of particular note, the recommendations of the services to be supported by a
4 universal service fund are varied. Staff supports Mr. Schoonmaker's proposed
5 definition. Although Staff does not specifically address the issue of which access
6 lines should be defined as universal services, judging by Staff's use of all access
7 lines in its calculations, it appears that Staff supports applying the definition to all
8 access lines. However, I leave it up to Staff to clarify its position on this issue.
9 Ameritech Illinois supports the list put forth by Mr. Schoonmaker, restricting
10 application of the definition of universal service to the primary line in a residence
11 and single business lines; Verizon supports Mr. Schoonmaker's list, seemingly
12 applying the definition of universal service to all access lines, and enhancing the
13 list of services to include standard white pages directory listings, and adding "of
14 the customer's choice" to "access to long distance carriers"; and WorldCom
15 supports Mr. Schoonmaker's list, adding some level of local usage and applying
16 the definition of universal service to primary residence access lines only.

17
18 In my direct testimony I listed various subgroups of access lines to which the
19 Commission could apply its definition of universal services, thereby eligible for
20 support. Parties have opted for one or another of these subsets, and the
21 Commission can choose at its option any of the given recommendations. Only if
22 the Commission adopts the modifications of the HAI5.0a input values
23 recommended by Dr. Clarke do I agree that the definition should be applied to all
24 access lines. Regarding the proposal of Verizon to supplement the list of services

1 with its suggestions, I recommend the Commission not adopt them at this time.

2 The Commission should initially structure a state high cost fund to support the
3 same services as adopted by the FCC. Support of further services can be
4 examined in the next phase of these proceedings, or at a later date, after the
5 Commission has had time to analyze the impact of its initial fund structure.

6
7 Regarding Mr. Sands' recommendation to include some level of local usage, this
8 may well be a moot issue. To the extent that the rural ILECs' local service is flat
9 rated, local usage is already included in the price of a network access line.

10 Regardless, I would again recommend the Commission not determine a specific
11 level of local usage at this time, but rather defer any consideration to a later date.

12
13 **Q. Do you have any general comments as to the method of calculating the**
14 **potential size of an Illinois state high cost fund?**

15
16 **A.** Yes. Staff witness Mr. Hoagg has proffered a methodology that provides for
17 adjusting the results of an Embedded Cost ROR Analysis by an HAI analysis.
18 Staff's adjustment is the same adjustment, albeit in reverse order, that I indicated
19 in my direct testimony I would address here, and should be adopted by the
20 Commission. Additionally, a "reverse adjustment" (i.e., an HAI analysis adjusted
21 by an ROR analysis) must also be adopted.

22
23 Without these adjustments, if a company were not in an over-earnings situation as
24 a result of the embedded cost ROR analysis, the company would be eligible to
25 receive the total revenue shortfall created by comparing an affordable rate to the

1 economic cost proxy. In some cases, this would provide an amount of fund
2 support that would put a company into an over-earnings situation. In other words,
3 in this situation, the fund would create and support over-earnings of a company
4 even though the overlay of the ROR analysis is intended to prevent this very
5 thing. Similarly, if the HAI analysis revenue shortfall were less than the ROR
6 analysis revenue shortfall, distributing funds equal to the ROR analysis revenue
7 shortfall would result in the fund providing support for services beyond those
8 included in the definition of universal services. It is necessary, then, to cap fund
9 support for any rural LEC at the smaller amount resulting from the two analyses.

10
11 With these adjustments, using Mr. Schoonmaker's proposed costs on an averaged
12 basis, a potential fund of \$11,959,239 is created rather than the \$14,567,114 fund
13 size Mr. Schoonmaker calculates in his supplemental direct testimony.

14
15 **Q. In what ways does the Staff proposed methodology differ from the one you**
16 **offered in your direct testimony?**

17
18 **A.** Mr. Hoagg recommends the company-specific HAI cost results be used rather
19 than average costs. Dr. Clarke discussed in his direct testimony why it is more
20 appropriate to use the average cost. However, in the event the Commission
21 determines that Staff's methodology of using company-specific proxy costs
22 should be adopted for purposes of satisfying the requirements of Section 13-
23 301(d), I have recalculated the results to reflect that methodology. Again using
24 Mr. Schoonmaker's proposed costs, but on a company-by-company basis, and
25 applying the analyses cap, a fund of the potential size of \$10,964,234 results.

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Q. Are there other differences between the two proposed methodologies?

A. In his direct testimony, Staff witness Mr. Koch discusses support of some and opposition to other of Mr. Schoonmaker's input value modifications. In his rebuttal testimony, Dr. Clarke responds to certain input modifications Mr. Koch has supported. Beyond Dr. Clarke's rebuttal, I will point out a glaring inconsistency on these issues within the testimonies filed by Staff.

For use in calculating economic costs, Mr. Koch adopts the cost of capital proposed by Mr. Alan Pregozen. Mr. Pregozen proposes costs of capital of 10.45%, 11.21%, and 12.60% for the Frontier LECs, small non-Frontier investor-owned LECs, and cooperative LECs, respectively. Mr. Pregozen states clearly that he is recommending these levels for use in the embedded cost ROR earnings analyses only, and offers the caveat that, "Staff would not necessarily endorse those costs of capital in future rate proceedings." (Staff Ex. 5.0, p. 2)

Yet, in parallel Staff testimony, Mr. Hoagg states, "A properly formulated forward-looking cost estimate will reflect the cost of an efficient competitor or new entrant." (Staff Ex. 1.0, p. 8) Consistent with this position, with which I concur, the Commission should adopt the cost of capital it has already adopted for use in a forward-looking economic cost study for Ameritech Illinois, i.e., 9.52%. The Commission should use this basic premise (i.e., of reflecting the cost of an

1 efficient competitor) as it determines whether to adopt or not adopt modifications
2 to the HAI 5.0a cost model in these proceedings.

3
4 Beyond the issue of input value modifications, I did not discern any other
5 significant differences between the two methodologies proposed.

6
7 **Q. — ~~Ms. Hegstrom, in your direct testimony you stated your intent to provide the~~**
8 **~~final calculations resulting from your proposed methodology, using the~~**
9 **~~default input values of HAI 5.0a. Have you done so?~~**
10

11 **A. —** Yes. I have provided Exhibit 5.1 to demonstrate the analysis of potential subsidy
12 included in the rural LECs' access services rates. As a result of my
13 recommendation to disallow funding to any company which "fails" this analysis,
14 and again overlaying the ROR analysis, my methodology would result in a fund
15 potentially sized at \$9,327,145.

16
17 **Q. — ~~In your direct testimony you also stated your intent to calculate the potential~~**
18 **~~size of a fund based on the input value modifications proposed by Dr. Clarke.~~**
19 **~~Have you done so?~~**
20

21 **A. —** Yes. Dr. Clarke has provided to me the economic costs for both the supported
22 services and switched access services resulting from his recommended
23 modifications to the HAI 5.0a input values. Exhibits 5.2 and 5.3 contain these
24 calculations. Employing my proposed methodology, with the ROR analysis
25 overlay, a potential fund sized at \$7,087,590 results. This is portrayed in Exhibit
26 5.4
27

1 ~~In addition to these calculations, I have also provided Exhibits 5.5 and 5.6 to~~
2 ~~demonstrate what size of fund would potentially result using company-specific~~
3 ~~HAI cost results as proposed by Staff. Use of Staff's methodology with the ROR~~
4 ~~analysis overlay would result in a potential fund of \$6,299,613, and is portrayed~~
5 ~~in Exhibit 5.7.~~

6
7 **Q. In direct testimony, Staff stated that use of its methodology would produce a**
8 **potential fund size of \$11,796,076. Why are your results different even if you**
9 **employ Staff's methodology?**

10
11 A. As I discussed above, Staff differs with AT&T's assessment of appropriate HAI
12 input value modifications. In addition, Staff has also included its proposed
13 transition to affordable rates in its calculations. In addition to not adopting Staff's
14 adopted HAI 5.0a input value modifications, I have not included a change of
15 affordable rates in any of my calculations, and would remind the parties that
16 whatever affordable rate the Commission adopts will have to be factored in to any
17 universal service fund support analyses.

18
19 **Q. Do you support Staff's recommendation for affordable rates for the rural**
20 **LECs?**

21
22 A. I do not offer a position on Staff's recommended rate levels. However, I would
23 point out that although Staff witness Mr. Staranczak discusses the need to include
24 the federal EUCL as part of the affordable rate, the federal EUCL rates have
25 already been deducted from the affordable rate levels to produce the Staff
26 recommended Option 3 rates of \$24 and \$27 for residence and business,
27 respectively. Currently, the federal EUCL of federal price cap regulated

1 companies is \$4.35 compared to \$3.50 for rate-of-return regulated companies.
2 Therefore, regardless of which option offered by the various parties the
3 Commission ultimately adopts, in order to remain consistent for comparison
4 purposes, the rates discussed are those without regard to the company's federal
5 EUCL.

6
7 Additionally, I do not oppose a transition to such recommended affordable rate
8 levels, as suggested by Staff.

9
10 **Q. Verizon suggests rural LECs increase access rates in order to become eligible**
11 **to receive any universal service support. Do you agree?**

12
13 A. No. Verizon completely misunderstands the methodology by which a company
14 may be deemed eligible for high cost fund support pursuant to Section 13-301(d),
15 as well as for what services they may receive support. Furthermore, Verizon's
16 recommendation could cause the rural LECs to establish subsidies in their access
17 rates, in violation of the federal TA96.

18
19 **Q. Can you explain?**

20
21 A. Yes. Dr. Beauvais compares the small company revenue shortfall calculated by
22 Mr. Schoonmaker with the calculated intrastate access revenue shortfall. Dr.
23 Beauvais suggests that if the rural LECs break the switched access federal mirror
24 and increase their access rates, a very substantial part, if not all, of the companies'
25 revenue shortfall can readily be remedied.

1 The flaw in Dr. Beauvais' logic is that he ignores the fact that the only revenue
2 shortfall that can be relieved by a state high cost fund is that associated with
3 services defined as universal services. The revenue shortfall calculated by Mr.
4 Schoonmaker is for universal services only. Thus, if a company were
5 experiencing a universal service revenue shortfall as a result of the economic cost
6 analysis, any revenue shortfall associated with universal services, even modified
7 by ROR analysis results, would still exist, and Dr. Beauvais' "solution" does not
8 solve the problem. More fundamental and problematic, if Dr. Beauvais is
9 recommending a company increase its switched access service rates to eliminate a
10 need for support for a company that generates universal service revenues short of
11 the associated universal services' economic costs, Dr. Beauvais' proposal would
12 establish implicit subsidies where they did not exist, or did not previously exist to
13 such an extent. This would be in clear contradiction of the intent of Section 13-
14 301(d)'s requirement to identify and remove implicit subsidies.

15
16 Despite all of this, Dr. Beauvais would have to agree that his perceived issue is
17 largely mooted with the revised economic cost proxies calculated by Dr. Clarke.
18 Furthermore, adoption of the overlay of ROR/HAI analyses removes Dr.
19 Beauvais' issue from these proceedings entirely.

20
21 **Q. Staff witness Mr. Koch indicates that other services could potentially be a**
22 **source of universal services subsidization. Does that impact in any way your**
23 **recommendation to discount any company's eligibility for fund support**
24 **based on access revenues exceeding access economic costs?**
25

1 A. If anything, it strengthens the appropriateness of doing so, as excessive access
2 revenues, even if they could be measured more accurately, might not be the sole
3 or major source of the company's subsidy. Because it would be inappropriate to
4 include other (non-universal service) services in the calculation of an affordable
5 rate, a conservative approach to distributing funds to rural LECs that have
6 excessive access revenues is recommended for an initial fund mechanism.

7
8 **Q. — As a result of your calculations, using costs calculated by Dr. Clarke, which**
9 **companies would not be eligible for fund support at this time?**

10
11 A. — ~~The list of companies not eligible at this time includes Adams, Clarksville, C R,~~
12 ~~Crossville, Egyptian, FC of Lakeside, FC of Mr. Pulaski, FC of Orion, Flat Rock,~~
13 ~~Geneseo, Grafton, Gridley, Hamilton, Henry County, Home, Kinsman, Leaf~~
14 ~~River, Leonore, Madison, Marseilles, McNabb, Moultrie, New Windsor, Odin,~~
15 ~~Oneida, Reynolds, Stelle, Viola Home, Woodhull and Yates City. It should be~~
16 ~~noted that this calculation results in slightly less than 70,000 rural access lines~~
17 ~~being subsidized. If the definition of universal service is restricted to only a~~
18 ~~subset of access lines, this number will decrease.~~

19 —
20 ~~Additionally, to reiterate the discussion from my direct testimony, the actual list~~
21 ~~of companies eligible to receive fund support can only be determined using the~~
22 ~~proxy costs, the affordable rates, the implementation of implicit subsidy~~
23 ~~indications, and the embedded cost ROR analysis results eventually adopted by~~
24 ~~the Commission in these proceedings.~~

1 **Q. — ~~Using Staff's methodology and Dr. Clarke's calculated HAI 5.0a costs, which~~**
2 **~~companies would not be eligible for fund support at this time?~~**

3
4 **A. — ~~The list of ineligible companies varies slightly. The list of companies not eligible~~**
5 **~~under Staff methodology includes Alhambra, Cambridge, Cass County,~~**
6 **~~Clarksville, C-R, Egyptian, El Paso, FC of Depue, FC of Mr. Pulaski, FC of~~**
7 **~~Orion, Geneseo, Glasford, Grafton, Gridley, Hamilton, Harrisonville, Henry~~**
8 **~~County, Home, Kinsman, LaHarpe, Leaf River, Leonore, Madison, Marseilles,~~**
9 **~~McNabb, Metamora, Moultrie, New Windsor, Odin, Reynolds, Stelle, Tonica,~~**
10 **~~Viola Home, Woodhull and Yates City. It should be noted that this calculation~~**
11 **~~results in slightly over 40,000 rural access lines being subsidized.~~**

12
13 **~~Neither of these lists reflect implementation of any proposed affordable rates.~~**
14 **~~Additional companies would be added to the ineligible list as they would not~~**
15 **~~require fund support or the same level of fund support once their local service~~**
16 **~~rates are transitioned to the affordable rate level.~~**

17
18 **Q. Will the FCC's recent Order concerning federal support for rural LECs**
19 **have any impact on your calculations?**

20
21 **A.** On May 10, 2001, the FCC issued an order in CC Docket No. 96-45, largely
22 adopting the framework proposed by the Rural Task Force. At the time of
23 testimony preparation, the FCC had not yet released its Order. However, based
24 on the Order Summary issued by the FCC, it appears that federal support levels
25 could increase. Once learned, any and all impacts would have to be factored in as
26 required by Section 13-301(d).

1

2 **Q. Turning now to the issue of a true-up to the funding of the Illinois DEM**
3 **Weighting Fund for the years 1998 through the current year 2001 extension**
4 **fund, how do you respond to the testimony of Ameritech and Verizon?**

5

6 A. Both Mr. O'Brien and Dr. Beauvais attempt to fabricate a basis for the
7 Commission to order that no true-up to the DEM Weighting Fund obligations
8 should occur. Although they construct some creative, though flawed, logic, the
9 fact of the matter is that the requirement for a true-up (1) has already been
10 adopted, (2) has already been ordered, and (3) has already been supported by the
11 testimony of both Mr. O'Brien and Dr. Beauvais.

12

13 **Q. Please explain.**

14

15 A. The 1997 Stipulated Agreement executed by both Ameritech Illinois and Verizon
16 (then GTE), and approved and adopted by the Commission contains the following
17 language:

18

19 15. Following the adoption of a Permanent Funding Method,
20 pursuant to a final and non-appealable Commission Order, there
21 shall be a "true-up" solely between and among the 1998 Funding
22 Carriers who have contributed to the 1998 Fund using the
23 Temporary Funding Method. The intent of the "true-up" is to, on
24 a proportionate basis, adjust among those 1998 Funding Carriers
25 payments made under the Temporary Funding Method to that of
26 the Permanent Funding Method for the period between January 1,
27 1998 up to the date the Permanent Funding Method is placed into
28 effect. The Parties agree, however, that there will be a "cap" on
29 the amount any 1998 Funding Carrier will have to pay into the
30 1998 Fund for the year 1998 as a result of a "true-up" from the
31 Temporary Funding Method to the Permanent Funding Method.
32 The Parties agree that the maximum amount any 1998 Funding
33 Carrier shall pay for the calendar year 1998 is one hundred fifty
34 percent (150%) of the amount that the 1998 Funding Carrier has
35 paid or would pay under the Temporary Funding Method. The
Parties recognize and agree that the "cap" associated with the

1 “true-up” as set forth above could affect the proportionate amount
2 of any refund a 1998 Funding Carrier may be entitled to receive.
3 The “true-up” should be administered by the Illinois Small
4 Company Exchange Carrier Association (“ISCECA”) or a
5 successor designated by the Commission.
6

7 The 1998 Stipulated Agreement, in extending the 1997 agreement, contains the
8 following language:

9 The Funding Carriers for the 1999 Fund and the 2000 Fund are
10 those Funding Carriers identified in amended paragraph 9 of
11 Attachment 2. The Temporary Funding Method, as described in
12 Attachment 2, will be used to fund the 1999 Fund and the 2000
13 Fund until a Permanent Funding Method is determined. (See
14 Attachment 2, paragraphs 7, 8 and 14) The “true-up” and “cap”
15 provisions described in paragraph 15 of Attachment 2 applicable to
16 the 1998 Fund are also applicable to the 1999 Fund and the 2000
17 Fund.
18

19 10. The issues addressed and resolved by this Stipulation relate
20 solely to DEM Weighting. The Parties acknowledge that there are
21 many important issues (concerning which individual parties have
22 different and conflicting positions) which will be addressed in
23 Consolidated Docket Nos. 97-0601 and 97-0602 and related
24 proceedings. The Parties further acknowledge the need to have the
25 issues raised and investigated in those proceedings and the
26 additional need to establish a Permanent Funding Method (see
27 Attachment 2) resolved in an expeditious and coordinated manner
28 taking into account the interrelationship of issues, the need for
29 coordination of federal and state actions, and the resources of the
30 Commission and the Parties. The Parties acknowledge that in
31 Phase 3 of Consolidated Docket Nos. 97-0601 and 97-0602 (see
32 paragraph 3 above) issues addressed in Phase 2, such as rate
33 rebalancing by rural local exchange carriers should be considered
34 together with other related issues and proposals, including the
35 impact of all such proposals on individual companies and their
36 respective customers.
37

38 And finally, in its Order extending the DEM Weighting Fund through September
39 2001, the Commission stated:

40 The Commission further concludes that the true-up and cap
41 provisions described in paragraph 15 of the 1998 Stipulation are

1 also applicable to the 2001 DEM Weighting Fund. Although
2 Ameritech, AT&T, WorldCom, and Sprint sought the continuation
3 of the fund with the elimination of or modifications to the true-up
4 and cap provisions, the Commission finds that insufficient reason
5 has been given for deviating from the funding methodology used
6 for the past three years.
7

8 (Docket No. 98-0679, Order On Reopening issued December 20, 2000, p. 4)

9 Throughout each of these proceedings, the Parties to the Stipulated Agreements
10 have agreed and the Commission has ordered that a true-up is required and shall
11 be accomplished. The only item yet to be determined is what the competitively
12 neutral basis for the Permanent Funding Method shall be.
13

14 **Q. How do you respond to Ameritech and Verizon's arguments that the**
15 **Commission has, in effect, already ruled on the issue of a Permanent Funding**
16 **Methodology?**
17

18 A. I simply direct these incumbent LECs to read page 3 of the Commission's Order
19 to Clarify in these proceedings, issued December 18, 2000, where it is stated:

20
21 The Commission cannot make a determination on the "permanent
22 funding methodology" at this time because the record in Phase I is
23 incomplete.
24

25 and

26 Although the Commission agreed with the LECs' contention that
27 the HCF and DEM Weighting fund cannot be combined to derive a
28 universal service fund under Section 13-301(d), the Commission
29 does not agree with the LEC's suggestion that the current funding
30 methodology should be deemed permanent for "true-up" purposes.
31 Instead, the Commission concludes that the permanent funding
32 methodology (and any associated "true-ups") will be addressed in
33 Phase II of the instant docket.
34
35

1 **Q. What if the Commission were to adopt a method of assessing fund**
2 **obligations on toll or access usage?**

3
4 A. First, the Commission is prohibited by Section 13-301(d) from adopting such a
5 requirement. Second, even aside from the current statutory requirements, the
6 Commission has already determined that a Permanent Funding Method is to be
7 competitively neutral. Per the Order adopting the initial Stipulated Agreement,
8 “[t]hose parties will have the opportunity to propose intrastate universal service
9 funding methodologies, which they believe to be consistent with the federal Act
10 and relevant FCC Orders.” (ICC Docket 97-0621, Order approved July 8, 1998,
11 page 8, emphasis added.) Third, as I discussed in my direct testimony,
12 assessment based upon toll usage is not competitively neutral because it
13 advantages a provider that provides little or no intrastate toll service. And finally,
14 no party in these consolidated proceedings has recommended such a basis for the
15 funding methodology to be used for a fund established pursuant to Section 13-
16 301(d). In fact, Mr. O’Brien argues that intrastate retail revenues be the basis for
17 assessments for the high cost fund “[i]n order for the funding for this new high
18 cost fund to be competitively neutral and nondiscriminatory.” (Ameritech Illinois
19 Ex. 2.0, p. 9, lines 5-7) Similarly, Dr. Beauvais flatly acknowledges that the
20 DEM Weighting Fund is not a competitively neutral funding arrangement.
21 (Verizon Ex. 4.0, p. 5, lines 69-70)

22
23 **Q. Ms. Hegstrom, you were involved in the negotiations that resulted in the**
24 **initial DEM Weighting Stipulated Agreement. Was there any discussion that**
25 **per the terms of the Agreement the parties could argue for the Commission**
26 **to disallow the true-up?**
27

1 A. No. In addition to negotiations resulting in the initial fund, I would add that I was
2 also involved in the negotiations that resulted in the 1999 and 2000 extensions of
3 the fund. In all negotiations, the parties agreed that rights of all parties were
4 reserved regarding what an appropriate permanent funding methodology should
5 be. However, it was clear among all parties that when the Commission
6 established a permanent funding methodology, a true-up would follow based on
7 that methodology. It is disappointing and frustrating to have negotiated in good
8 faith with companies such as Ameritech and Verizon, believing they were also
9 negotiating in good faith, and now discover they are attempting to get the
10 Commission to "give them an out." It is especially disingenuous for Ameritech to
11 now try to argue that the true-up could be based on a method that does not comply
12 with the federal principle of competitive neutrality and non-discrimination, and to
13 even go so far as to attempt to convince the Commission that it might not be in
14 the public interest to allow the implementation of the terms of the Stipulated
15 Agreements. Specifically, it is a blatant violation of the terms of the Stipulated
16 Agreements to suggest that the Commission should and could dismiss the true-up
17 simply because the Commission once termed the DEM Weighting Fund an access
18 revenue replacement fund. This violation is especially egregious when one
19 considers the fact that Mr. O'Brien's argument is invalidated by the precedent
20 established by the FCC. That is, in removing the interstate DEM Weighting
21 dollars from interstate access services, and transferring them to the federal
22 universal service fund, the FCC replaced access revenues via a universal service

1 fund, dollar for dollar, and required fund obligations to be assessed in a
2 competitively neutral manner.

3
4 **Q. How do you respond to Mr. O'Brien's assertion that funding for the DEM**
5 **Weighting Funds was competitively neutral?**

6
7 A. It is easy to understand Mr. O'Brien's or any incumbent LEC's incentive to
8 characterize such funding methods as competitively neutral. However, the fact of
9 the matter is that Mr. O'Brien is confusing *revenue* neutrality, a term very
10 familiar to incumbent LECs, with *competitive* neutrality. Mr. O'Brien need only
11 review how the federal funding methodology was designed relative to revenue
12 neutrality to understand that it is not synonymous with competitive neutrality.

13
14 **Q. On a side note, do you agree with the way Mr. O'Brien describes the cap that**
15 **is to be applied to the true-up?**

16
17 A. No. Mr. O'Brien describes the 50% cap on the true-up as limiting a carrier's
18 obligation such that it need not pay more than half of what the true-up amount
19 would have been absent a cap. Mr. O'Brien appears to have simply misstated his
20 understanding in his current direct testimony. In his direct testimony filed in the
21 initial phase of these consolidated proceedings, Mr. O'Brien correctly described
22 the purpose of the cap as follows:

23 There was, however, a cap placed on the true-ups, whereas no
24 company would be required to pay a true-up of greater than 50% of
25 its 1998 funding requirement under the temporary funding
26 methodology.
27

1 Ameritech Illinois Ex. 1.0, p. 10, lines 2-5. This is the correct application of the
2 cap, and is supported by the testimony of Sprint and WorldCom witnesses in these
3 proceedings.

4
5 **Q. In your direct testimony, you recommended a third phase in these**
6 **proceedings in order to investigate other issues. Have any other parties**
7 **suggested this as well?**

8
9 A. No. However, I believe that several issues discussed by various parties could and
10 should be deferred to a subsequent investigation, including the opportunity for an
11 audit of any state fund, the appropriateness of seeking a neutral third party to
12 administer a state high cost fund, as well as the issues I listed in my direct
13 testimony.

14
15 **Q. Does this conclude your rebuttal testimony?**

16 A. Yes, it does.

**STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION**

**ILLINOIS INDEPENDENT TELEPHONE
ASSOCIATION**

**Petition for initiation of an investigation
of the necessity of and the establishment
of a Universal Service Support Fund
in accordance with Section 13-301(d)
of the Public Utilities Act**

**ILLINOIS COMMERCE COMMISSION
ON ITS OWN MOTION**

**Investigation into the necessity of and,
if appropriate, the establishment of a
universal support fund pursuant to
Section 13-301(d) of the Public Utilities Act.**

00-0233

00-0335

REBUTTAL AFFIDAVIT OF AT&T WITNESS CATE HEGSTROM

1. My name is Cate Hegstrom and on May 31, 2001, I filed written Rebuttal Testimony on behalf of AT&T Communications of Illinois, Inc. ("AT&T") in the above-captioned docket. It is my understanding that all parties have waived cross-examination of me and I submit this affidavit to have my pre-filed written testimony admitted into evidence.

2. My Rebuttal Testimony is identified as AT&T Exhibit 5.0 and consists of twenty one (21) pages of questions and answers.

3. AT&T Exhibit 5.0 was prepared by me or at my direction.

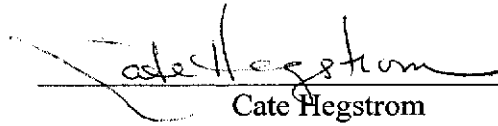
4. I have no changes to make to AT&T Exhibit 5.0.

5. If asked again the same questions that appear in AT&T Exhibit 5.0, I would give the same answers.

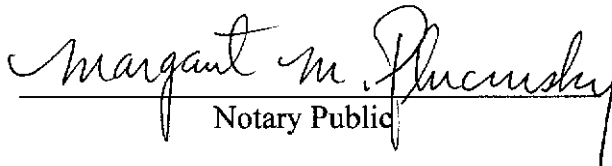
OFFICIAL FILE
ILL. C. C. DOCKET NO. 00-0233/0335
AT&T filed Exhibit No. _____
Page 7-20-01 *CB*

I hereby swear that the foregoing information in this affidavit and my answers in my pre-filed written testimony (AT&T Exhibit 5.0) are true and correct.

Dated: July 12, 2001


Cate Hegstrom

Subscribed and Sworn to before me
this 12th day of July, 2001.


Notary Public

